Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Runner	Analyst:	Gail Hall	Bill Number:	SB 359
Related Bills:	See Legislative History	Telephone:	845-6111	Amended Date:	May 14, 2007
		Attorney:	Daniel Biedler	Sponsor:	

SUBJECT: Business Income Apportionment/Members Of Apportioning Trade Or Business May Elect To Utilize One Of The Alternative Formulas/Research Expenses Credit/20% Of Excess Qualified Expenses/Conformity To Election Of Alternative Incremental Credit

SUMMARY

Under the Personal Income Tax and Corporation Tax laws, this bill would do the following:

- Modify the credit for research expenses to 20% of the excess of the qualified research expenses.
- Modify the alternative incremental research credit (AIRC).

Under the Corporation Tax Law, this bill would change the method used by eligible companies to calculate their California business income.

This bill would also add a provision to the Sales and Use Tax Law (SUTL). This analysis will not address these changes as they do not impact the department or state income tax revenue.

The analyses of the bill as introduced on February 20, 2007, and amended on April 9, 2007, no longer apply.

SUMMARY OF AMENDMENTS

The May 14, 2007, amendments made the following changes:

- Removed the provisions of the bill relating to the Joint Strike Fighter and Crew Exploration Vehicle credits.
- Removed the provisions of the bill relating to the motion picture and commercial production credits.
- Removed the provisions of the bill that would allow certain taxpayers to elect to use a three-factor, quadruple-weighted sales apportionment formula, remove “extractive business activities” from the definition of a qualified business activity, and add other miscellaneous provisions relating to the apportionment formula.
- Added provisions that would allow eligible corporations to elect alternative apportionment methods.
- Conformed to the federal research and development credit and AIRC percentages.

Board Position:			Department Director	Date
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_______ N	_______ OUA	___X___ PENDING		

PURPOSE OF THE BILL

According to the author's staff, the purpose of this bill is to accomplish the following:

1. Increase economic productivity in California.
2. Encourage certain industries to invest in California.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective immediately upon enactment. This bill provides the following operative dates for each of the following provisions:

1. Research Expense Credit: Taxable years beginning on or after January 1, 2007.
2. Alternative Apportionment Methods: Taxable years beginning on or after January 1, 2007.

POSITION

Pending.

SUMMARY OF ECONOMIC IMPACT

Estimated Revenue Impact of SB 359 Effective for tax years BOA 1/1/2007 Enacted by 6/1/2007				
	2007-08	2008-09	2009-10	2010-11
Research Expense Credit	-$125 Million	-$160 Million	-$170 Million	-$175 Million
AIRC Rates	-$5 Million	-$5 Million	-$5 Million	-$5 Million
Alternative Apportionment Methods	-$1 Billion	-$1 Billion	-$1 Billion	-$1 Billion
Total	-$1.130 Billion	-$1.165 Billion	-$1.175 Billion	-$1.180 Billion

ANALYSIS

1. <u>RESEARCH EXPENSE CREDIT</u>

<u>FEDERAL/STATE LAW</u>

Existing federal law allows taxpayers a research credit that is combined with several other credits to form the general business credit. The research credit is designed to encourage companies to increase their research and development activities.

To qualify for the credit, research expenses must qualify as an expense or be subject to amortization, be incurred in the U.S., and be paid by the taxpayer. The research must be experimental or laboratory research and pass a three-part test as follows:

1. Research must be undertaken to discover information that is technological in nature. The research must rely on the principles of physical, biological, engineering, or computer sciences.
2. Substantially all of the research activities must involve experimentation relating to quality or to a new or improved function or performance.

3. The application of the research must be intended for developing a new or improved business component. This is a product, process, technique, formula, or invention to be sold, leased, or licensed, or used by the taxpayer in a trade or business.

Ineligible expenses include seasonal design factors; efficiency surveys; management studies; market research; routine data control; routine quality control testing or inspection; expenses incurred after production; or development of any plant, process, machinery, or technique for the commercial production of a business component unless the process is technologically new or improved.

Current federal law allows taxpayers to elect an AIRC method for computing the research credit that involves using different base amounts and fixed-base percentages. The following are the credit percentages for the AIRC:

- 3.0% (1.49% for California) applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fixed-base percentage of 1% but do not exceed a base amount computed using a fixed base percentage of 1.5%.
- 4.0% (1.98% for California) applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fixed-base percentage of 1.5% but do not exceed a base amount computed using a fixed base percentage of 2.0%.
- 5.0% (2.48% for California) applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fixed-base percentage of 1% but do not exceed a base amount computed using a fixed base percentage of 2.0%.

The federal credit does not apply to any expenses paid or incurred after December 31, 2007.

California conforms to the federal credit with the following modifications:

- The state credit is not combined with other business credits.
- Research must be conducted in California.
- The credit percentage for qualified research expense in California is 15% versus the 20% federal credit.
- The credit percentage for basic research payments in California, limited to corporations, is 24% versus the 20% federal credit.
- The percentages for the state alternative incremental research portion of the credit are less than the federal credit. (See percentages listed above.)

The California research expense credit is allowed for taxable years beginning on or after January 1, 1987, and is permanent without regard to whether the federal credit is operative.

<u>THIS PROVISION</u>

This provision would conform state law to the 20% federal research and expense credit and to the federal AIRC percentages.

LEGISLATIVE HISTORY

AB 751 (Lieu, 2007/2008) would increase the research credit for increasing qualified research expenses from 15% to 20% for taxable years beginning on or after January 1, 2007, and would also fully conform to the federal alternative incremental research expenses credit for taxable years beginning on or after January 1, 2007. This bill is currently in the Assembly Revenue and Taxation Committee.

AB 2032 (Lieu, 2005/2006) would have increased the amount of the qualified research expense credit from 15% to 18%. AB 2032 failed to pass out of the Assembly Revenue & Taxation Committee.

AB 2567 (Arambula, 2005/2006) would have conformed the amount of the qualified research expense credit to the amount allowed at the federal level. AB 2567 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 483 (Harman, 2001/2002) and SB 1165 (Brulte, 2001/2002) would have increased the credit for qualified research expenses from 15% to 20%. AB 483 was held in the Senate Revenue and Taxation Committee. SB 1165 failed to pass out of the originating house by the constitutional deadline.

AB 511 (Stats. 2000, Ch. 107) increased the state credit for qualified research expense from 12% to 15%.

OTHER STATES' INFORMATION

The states surveyed include *Florida*, *Illinois*, *Massachusetts*, *Michigan*, *Minnesota*, and *New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida allows corporate taxpayers to claim a corporate income tax credit for tax years beginning on or after January 1, 2007, for certain "eligible costs" for renewable energy technologies investment. *Florida* does not have a comparable credit for personal income taxpayers because *Florida* has no state personal income tax.

Illinois corporate and individual taxpayers may claim an income tax credit for qualified expenditures that are used for increasing research activities in *Illinois*. The credit equals 6½% of the qualifying expenditures.

Massachusetts allows corporate taxpayers to claim an income tax credit for qualified expenditures that are used for increasing research activities in *Massachusetts*. The credit is 15% of the basic research payments and 10% of qualified research expenses conducted in *Massachusetts*.

Minnesota allows corporate taxpayers a credit equal to 5% for qualified research expenses up to $2 million. The amount of the credit is reduced to 2.5% for expenses exceeding the first $2 million.

Michigan allows corporate taxpayers a credit for pharmaceutical research and for a percentage of the compensation for services paid by the taxpayer that is engaged in research and development of a hybrid system for propelling motor vehicles. An eligible taxpayer may claim a credit against the Single Business Tax equal to 6.5% of the excess of qualified research expenses paid in the tax year that relate to pharmaceutical-based business activity in *Michigan* paid during the three immediately preceding tax years.

Beginning in 2005, *New York* allows a credit for qualified emerging technology companies. The credit is equal to 18% of the cost of research and development property, 9% of the qualified research expenses, or the costs of high-technology training expenditures paid by the taxpayer. The credit is limited to $250,000 per taxable year.

FISCAL IMPACT

The provision would not significantly impact the department's costs.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

Estimated Revenue Impact of SB 359 Effective for Tax Years BOA 1/1/2007 Enacted by 6/1/2007				
	2007-08	2008-09	2009-10	2010-11
Research Expense Credit	-$125 Million	-$160 Million	-$170 Million	-$175 Million
AIRC	-$5 Million	-$5 Million	-$5 Million	-$5 Million
Total	-$130 Million	-$165 Million	-$175 Million	-$180 Million

The revenue impact of this provision is estimated to be as shown in the table above. This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

<u>Revenue Discussion</u>

The revenue loss due to increased research expense credit rate was estimated using a corporate and personal income tax model based on the 2001-04 Franchise Tax Board (FTB) samples of corporate tax returns. For each corporation in the sample of corporate tax returns, the tax liabilities under the current and proposed laws were simulated taking into account the entity's taxable income, net operating losses, qualified research expenses, the research expense credit rates, and carryover credits. Not all additional research credit generated in a particular year could be used in that year. Taxpayers without sufficient tax liability would not be able to fully use the additional credit. Unused credit would be carried forward to subsequent years.

The unused research expense credit is currently in excess of $8 billion. The corporate and personal income tax model results show that the proposed increased research expense credit rate would generate $580 million additional credit in 2004; however, it is estimated that only $115 million of this amount could be used in reducing tax liability for the same tax year.

AIRC currently accounts for about 2% of the research expense credit claimed. The percentage increases in the AIRC rates under this provision are higher than that of the research expense credit rate. Therefore, it was assumed that the revenue loss due to higher AIRC rates would be about 5% of the loss from higher regular research and development credit rate. The results from the tax model were expanded from the samples to corporate population.

The personal income tax revenue impact in future years as a fraction of the corporate revenue impact is assumed to be equal to the ratio of personal income tax research expense credits to corporate qualified research expense credits in 2004. The percentage in 2004 was 4%.

2. ALTERNATIVE APPORTIONMENT METHODS

FEDERAL/STATE LAW

Federal law is inapplicable because its method of taxing corporations is not based on whether the corporation is doing business within and without any particular state.

California has adopted the Uniform Division of Income for Tax Purposes Act, (UDITPA), with certain modifications, to determine how much of an apportioning taxpayer’s total income, which is earned from activities both inside and outside of California, is attributed to California and subject to California franchise or income tax. UDITPA uses an apportionment formula to determine the amount of “business” income attributable to California.[1]

The apportionment formula consists of property, payroll, and sales factors. The property factor includes tangible property owned or rented during the taxable year; the payroll factor includes all forms of compensation paid to employees; and the sales factor is double-weighted and generally includes all gross receipts from the sale of tangible and intangible property.

[1] “Business income attributable to California” is a taxpayer’s “business income” multiplied by its California apportionment formula. Revenue and Taxation Code (R&TC) section 25120(a) defines “business income” as income arising from transactions and activities in the regular course of the taxpayer’s trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer’s regular trade or business operations." R&TC section 25120(d) defines “nonbusiness income” as all income other than business income. In general, "business income" is income arising in the normal course of the taxpayer's business or from assets used in the normal course of the taxpayer's business.

The calculation of the apportionment formula and California business income is illustrated below.

$$\frac{\dfrac{\text{Average CA Property}}{\text{Average Total Property Everywhere}} + \dfrac{\text{CA Payroll}}{\text{Total Payroll Everywhere}} + \left(2 \times \dfrac{\text{CA Sales}}{\text{Total Sales Everywhere}}\right)}{4} = \text{California Apportionment Formula}$$

X Total Business Income
= California Business Income

For taxable years beginning on or after January 1, 1993, the apportionment formula for most taxpayers has been a three-factor apportionment formula consisting of property, payroll, and double-weighted sales (three-factor, double-weighted sales). An exception to this rule exists for taxpayers that derive more than 50% of their gross business receipts from conducting a "qualified business activity." These taxpayers are required to use a three-factor, single-weighted sales, apportionment formula. For this purpose, a qualified business activity is defined as an agricultural, extractive, savings and loan, and banking or financial business activity. In addition, current law requires that once a determination has been made that the apportioning trade or business is involved in a qualified business activity, the entire apportioning trade or business uses the same weighting, regardless of whether the particular entity was involved in a qualified business activity.

State law permits a departure from the standard apportionment provisions only in limited and specific cases,[2] and recognizes that the standard apportionment provisions are not appropriate when applied to certain industries and types of transactions, in which case special apportionment provisions exist for those situations.[3]

THIS PROVISION

This provision would create two alternative apportionment methods a corporation may elect to utilize that would deviate from the standard apportionment formulas described under the Current State Law section above.

[2] R&TC section 25137.
[3] California Code of Regulations (CCR), title 18, Section 25137.

Alternative #1 – Sales Factor

For each $250 million of qualified expenditures made by a member of an apportioning trade or business after January 1, 2007, an additional sales factor would be added to the numerator of the apportionment formula and the denominator of the apportionment factor would be increased by one. (See Appendix A for examples illustrating Alternative 1).

- The apportioning trade or business, or a subgroup thereof, must submit and certify with each tax return filed a summary of the qualified expenditures.
- Qualified expenditures shall include all of the following:
    1) Capital expenditures for real and tangible personal property located in California.
    2) Expenses incurred to acquire, develop, or license intellectual property in California.
    3) Research and development expenses incurred in California.
    4) Expenses incurred to develop, enhance, or maintain real property and tangible personal property located in California.
    5) Capitalized rent paid in California in excess of the prior year.
    6) Compensation and benefits paid to employees in California in excess of the prior year.
    7) Payments to independent contractors and payroll companies for work performed in California in excess of the prior year.
    8) Training costs incurred in California.
    9) Costs incurred in providing a basic level of health care to employees in California, as defined in the Knox-Keene Health Care Service Plan Act, in excess of the prior year.
    10) Expenditures incurred in connection with funding research at a four-year public or private college or university located in California.

Alternative #2 – Property and Payroll Factor

A corporation may elect to adjust its property and payroll factors as follows:

- Property shall be excluded from the numerator of the property factor if it is in excess of the value of the taxpayer’s real and tangible personal property owned or rented and used in California in the base year.
- The amount of compensation paid by a taxpayer that is in excess of the amount of total compensation paid in the state in the base year would be excluded from the numerator of the payroll factor. Compensation in the base year excludes extraordinary events such as deferred compensation payouts or stock option exercises.
- “Base year” is defined as the year immediately preceding the year of election.
- The member of the apportioning trade or business, or a subgroup thereof, must submit and certify with each tax return filed a summary of the new investment made in California.

See Appendix B for examples illustrating Alternative #2.

Other Provisions

- The election for either Alternative #1 or #2 must be made by attaching a statement to the original return and by specifying the method of adjusting the apportionment factor. The election may be terminated either by the taxpayer with the permission of FTB, or by FTB if the taxpayer fails to submit and certify the required information.
- Electing Alternatives #1 or #2 would not be construed to terminate a water's-edge election, or construed to allow a change or adjustment to the water's-edge election.
- FTB would be required to prescribe rules and regulations to implement the provisions of this bill.
- The provisions of this bill are severable, so that if any provision or its application is held invalid, that invalidity shall not affect other provisions that can still be given effect without the invalidated provision.
- It is the intent of the Legislature that the sales factor used in any special apportionment rules under section 25137 of the Revenue and Taxation Code would still apply and would not be modified by the bill's provisions.

IMPLEMENTATION CONSIDERATIONS

1. The provision provides that property shall be excluded from the numerator of the property factor if it is in excess of the value of the property used in the state in the base year. The department has interpreted this requirement to mean the numerator of the property factor would be zero if the excess requirement is met. If the author meant for only the incremental amount of property over the base year value would be excluded from the numerator of the property factor, amendments should be considered.
2. The provision lacks a definition for "value of the taxpayer's real and tangible personal property owned or rented" (i.e., cost, fair-market value) and "the amount of compensation" relating to the payroll factor. The department would be unable to implement this provision without a definition.
3. It is unclear how the apportionment formula for a combined report (group tax filing) would be calculated when members of the combined group make different elections under the proposed two new apportionment methods. Current law lacks provisions that allow different members of the same apportioning trade or business to utilize different sales factor weighting. The author should consider providing clarity for elections made by members of a combined group.
4. The provision lacks detailed guidelines for FTB to determine when an election is terminated. The author should consider creating an election similar to the water's-edge election that binds the taxpayer to the water's-edge election for seven years, upon the expiration of which would allow the taxpayer to terminate it.
5. The provision appears to grant FTB mandatory legislative rulemaking authority. The author should consider making the grant discretionary and clarify this is legislative rulemaking authority to ensure effective implementation of the provisions of the bill relating to the new elections for calculating the apportionment formula.

6. On page 79, line 8, the bill provides that the entire business income of the group shall be apportioned using a three factor, single-weighted sales factor or a three factor, double-weighted sales factor apportionment formula. This appears to be in conflict with the allowance of subgroups for the proposed alternative apportionment formulas. The author should consider using the same rules for all the methods for determining the apportionment formula or clarify the difference.

TECHNICAL CONSIDERATIONS

The department has identified the following technical considerations. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

1. On page 76, line 21, it appears "in this state" should be inserted after "compensation paid." If the author meant for the current year's compensation amount to be the amount paid in the state, an amendment is necessary.
2. On page 76, line 36, the author should consider adding "timely filed" before "original return" to avoid unintended tax planning opportunities.

LEGISLATIVE HISTORY

AB 1591 (Ma, 2007/2008) contains similar apportionment provisions to those found in SB 359 and would create two alternative apportionment methods that a corporation may elect to utilize that would deviate from the standard apportionment formulas. AB 1591 is currently in the Assembly Revenue and Taxation Committee.

AB 1037 (Frommer, 2005/2006), as amended on August 7, 2006, would have created a three-factor, quadruple-weighted sales, apportionment formula for certain industries. AB 1037 was held in the Senate Revenue and Taxation Committee.

AB 2590 (Campbell, 2003/2004) and AB 2560 (Vargas, 2001/2002) would have replaced the three-factor, double-weighted sales apportionment formula used by most corporations with a single-factor apportionment formula based solely on sales. Exceptions to using the single-factor formula would have included: (1) taxpayers that had an average of property and payroll in California in excess of sales that did not meet certain employment requirements would use the three-factor, double-weighted sales formula, and (2) taxpayers that derive more than 50% of their gross business receipts from extractive activities could have used either the single-factor sales formula or the three-factor, single-weighted sales formula. AB 2590 and 2560 were held in Assembly Appropriations.

AB 1642 (Harmon, 2001/2002) and SB 1014 (Johnson, 2001/2002) would have changed the apportionment formula used to determine the amount of business income taxable by California to a single-factor apportionment formula based on sales and allowed extractive businesses to choose either the current three-factor formula based on property, payroll, and sales, or use the new single-factor formula. AB 1642 died pursuant to Article IV, Section 10(c) of the Constitution; SB 1014 was returned to the Secretary of Senate pursuant to Joint Rule 56.

OTHER STATES' INFORMATION

The states surveyed include *Florida*, *Illinois*, *Massachusetts*, *Michigan*, *Minnesota*, and *New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

General research was performed to determine how these other states "weight" their apportionment formula.

Florida's apportionment formula consists of 25% property, 25% payroll, and double-weighted sales factor, with some exceptions for specialized industries.

Massachusetts's apportionment formula for eligible corporations consists of 25% property, 25% payroll, and a double-weighted sales factor.

Illinois began using the single sales factor for tax years ending on or after December 31, 2000. The single sales factor formula is used by corporations deriving business income from the state, rather than being determined by a corporation's principal business activity code.

Michigan's apportionment formula consists of 5% property, 5% payroll, and 90% sales.

Minnesota's apportionment formula consists of 12.5% property, 12.5% payroll, and 75% sales for tax years beginning before 2007. In 2005, *Minnesota* enacted legislation to phase in a sales-only formula over an eight-year period beginning in 2007.

New York utilizes a business allocation formula to assign income from business capital to *New York*. For tax year 2006, *New York* will begin the process of phasing in a new, single-factor allocation formula based on in-state receipts. The single-factor allocation formula will be phased-in as follows: (1) for tax year 2006, the business allocation formula will be equal to 20% property, 60% sales, and 20% payroll; (2) for tax year 2007, the business allocation formula will be equal to 10% property, 80% sales, and 10% payroll; and (3) for tax years beginning on or after January 1, 2008, the business allocation formula will consist of 100% sales.

FISCAL IMPACT

The department's costs to administer this provision cannot be determined until the department's implementation concerns have been resolved. If the department is required to implement subgroups filing combined within a unitary combined group, forms and information systems may need changes.

ECONOMIC IMPACT

Revenue Estimate

The revenue impact of this provision is estimated to be as shown in the following table:

Estimated Revenue Impact of AB 1591 Effective for tax years BOA 1/1/2007 Enacted by 6/1/2007			
2007-08	2008-09	2009-10	2010-11
-$1 Billion	-$1 Billion	-$1 Billion	-$1 Billion

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

It was determined that for every corporation that would benefit from a hyper-weighted sales factor (Alternative 1), it would benefit even more from the second alternative, which results in an elimination of the property factor numerator. Therefore, the focus of this estimate is on Alternative 2.

To estimate the revenue impact of Alternative 2, the impact of allowing all corporations to exclude the numerator of their property factor while keeping the denominator unchanged was estimated. Simulations based on samples of corporation tax returns for the tax years 2003, 2004, and 2005 indicate the impact of Alternative 2 is a revenue loss of approximately $2.28 billion for the tax year 2007. It is assumed that 50% of all apportioning taxpayers would qualify for Alternative 2, and the estimated revenue impact of this provision is a revenue loss of $1.14 billion ($2.28 x 0.5 = $1.14 billion), rounded to $1 billion, in 2007. Because of the size of the revenue loss for this aspect of Alternative 2, the possible revenue impact from a reduction in the payroll factor was disregarded. In addition, this estimate disregards potential changes in taxpayer behavior, such as the potential for a current California nonapportioning corporation to develop nexus with some other state to take advantage of Alternative 2 to exclude property from the numerator of the property factor.

LEGAL IMPACT

This provision would preface whether a taxpayer may use Alternative 1 or 2 based on the level of activity in this state, which could be subject to constitutional challenge under the Commerce Clause of the United States Constitution. Possible constitutional issues found in the provision include the investment of qualified expenditures, property, and payroll in the state.

ARGUMENTS/POLICY CONCERNS

1. The intended effect of encouraging business to expand in California would only apply to apportioning trades or businesses if this provision were adopted. A business located in California that is wholly in-state would receive no benefit from this provision because wholly in-state businesses do not apportion their income.
2. The allowance of sub-grouping could lead to different filing positions on a yearly basis determined solely on whether the tax effect is greater for a member to utilize the base year computation for property or payroll versus the sales factor effect of multiple weighting.
3. The provision includes maintenance costs as qualified costs. This appears to be at odds with the purpose of the provision to expand California business. These costs would already be incurred and are not a new activity of the taxpayer, yet they are treated as such.
4. The value of property test lacks a provision for recapture. A taxpayer could purchase property at the end of the year to meet the test's requirement, and then return the property after the test is met; alternatively, the members of a unitary group could continuously dispose of the same property to each member of their combined reporting group to qualify multiple members for the election utilizing the same property.

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APPENDIX A
SB 359
EXAMPLES OF ALTERNATIVE 1 – SALES FACTOR

SCENARIO A:

Facts

Property Factor = 20%

Payroll Factor = 20%

Sales Factor = 80%

Made $250 Million of qualified expenditures

Under current law uses a double-weighted sales factor

Apportionment percentage using current law:

(Property 20% + Payroll 20% + Sales 80% + 80%)/4 = **50%**

Apportionment percentage using Alternative #1:

(Property 20% + Payroll 20% + Sales 80% + 80% + 80%)/5 (4 + 1) = **56%**

SCENARIO B:

Facts

Property Factor = 80%

Payroll Factor = 80%

Sales Factor = 20%

Made $250 Million of qualified expenditures

Under current law uses a double-weighted sales factor

Apportionment percentage using current law:

(Property 80% + Payroll 80% + Sales 20% + 20%)/4 = **50%**

Apportionment percentage using Alternative #1:

(Property 80% + Payroll 80% + Sales 20% + 20% + 20%)/5 (4 + 1) = **44%**

APPENDIX B
SB 359
EXAMPLES OF ALTERNATIVE 2 – PROPERTY AND PAYROLL FACTORS

SCENARIO A:

Facts

Base Year Value of Property Used In CA = $200,000
Base Year Value of CA Payroll = $100,000
Uses double-weighted sales factor
Property Factor = 20%: Current year value of property equals $250,000
Payroll Factor Numerator = $200,000
Payroll Factor Denominator = $1,000,000
Payroll Factor = 20%
Sales Factor = 80%

Apportionment percentage using current law:

(Property 20% + Payroll 20% + Sales 80% + Sales 80%)/4 = **50%**

Apportionment percentage using Alternative #2:

(Property 0% + Payroll $\frac{\$200,000 - \$100,000}{\$1,000,000}$ = 10% + Sales 80% + 80%)/4 = **42.5%**

SCENARIO B:

Facts

Base Year Value of Property Used In CA = $800,000
Base Year Value of CA Payroll = $800,000
Uses double-weighted sales factor
Property Factor = 80%: Current year value of property equals $850,000
Payroll Factor Numerator = $850,000 Payroll Factor Denominator = $1,000,000
Payroll Factor = 85%
Sales Factor = 20%

Apportionment percentage using current law:

(Property 80% + Payroll 85% + Sales 20% + Sales 20%)/4 = **51.25%**

Apportionment percentage using Alternative #2:

(Property 0% + Payroll $\frac{\$850,000 – 50,000}{\$1,000,000}$ = 80% + Sales 20% + 20%)/4 = **30%**